CHiLD POVERTY ACTION GROUP

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Submission to The Finance and Expenditure Committee,

Financial Service Providers (Registration and Dispute Resolution) Bill

We would like to be heard in support of this submission

We thank you for the opportunity to submit our views on this review. Child Poverty Action Group comprises a group of academics and workers in the field dedicated to achieving better policies for children. Our reports *Our Children: The priority for policy* 2001, and 2003 can be found with other background material at our web site.

The aims of our organisation are:

- The development and promotion of better policies for children and young people.
- Sharing information and connecting with other groups with similar concerns.
- Elimination of child poverty in Aotearoa New Zealand by 2015

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Introduction

[1] This Bill is unusual in that the various political parties are in agreement as to the urgency of its purpose: regulation in the financial sector.[1] Given this unusual circumstance, Child Poverty Action Group encourages the committee to consider this Bill from the perspective of its impact on children and low income and vulnerable families. Our early investigations into poverty levels suggested that from the early 1990s one third of our children under the age of 15 were being raised in families that did not have sufficient disposable income to ensure their full development.[2] In addition, the Ministry of Social Development in *The Social Report*, 2006,[3] numerous NGOs, and the media, have regularly gathered evidence and reported that children are disproportionately among our poorest citizens. A deterioration in the economic position of children from low income families and the consequent social costs can be partially attributed to changes in demography and the labour market, and significantly attributed to a tax regime that over time has led to the unfair shifting of the tax burden to the poor.[4] As we argued in our 2007 Submission on the Review of Financial Products and Providers, in recent years the lack of adequate consumer protection in the financial sector must carry a share of the blame for the worsening economic position of children. Financial products and providers impact on children indirectly because their parents and caregivers are the investors and consumers referred to in the Bill. This Submission urges the New Zealand Government to ensure the legislation does not have a negative impact on children or on low income or vulnerable families.

[2] We strongly support the intention of the Bill to mandate membership of an approved dispute resolution scheme for all financial service providers, and for the schemes to either be fully funded by industry or, in the case of the reserve scheme, by a levy on members. We also support including small businesses in the broad definition of

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[1] First Reading of the Bill reported in Hansard, Volume:644;Page:14001.

[2] St John, S., M. C. Dale, M. O'Brien, A. Blaiklock, S. Milne. (2001). *Our Children: the priority for policy*. Auckland, Child Poverty Action Group Inc.

[3] Ministry of Social Development (2006). *The Social Report*. Wellington, Ministry of Social Development, Government of New Zealand.

[4] Child Poverty Action Group (2003). *Our Children: The Priority for Policy* (2nd edition). Auckland, Child Poverty Action Group.

consumer, as the existing Banking Ombudsman and Insurance and Savings Ombudsman schemes do. Our submission focuses principally on five aspects of the Bill:

- The proposed 4 year time lag before the scheme is fully implemented
- The proposed imposition of a charge on consumers for dispute resolution
- The need for consumer representation in schemes' governance
- The risks posed by multiple schemes
- The need for public awareness of the consumer protections introduced

(1) The proposed 4 year time lag before the scheme is fully implemented

[3] The Explanatory Note to the Bill states:

> *It is intended that the register be in place in 2010. There will be a transitional period, intended to be 2 years, to allow those affected time to ensure compliance.*

If the register is in place in 2 years, and is followed by a 2-year transition period, then the regulation will not be fully implemented until 2012.

[4] And S2 of the Bill[5] states:

> ***2 Commencement***
>
> ***(1) Part 2 and Section 44*** *come into force on a date to be appointed by the Governor-General by Order in Council, and 1 or more Orders in Council may be made appointing different dates in respect of different types of financial service providers*
>
> ***(2)*** *The rest of this Act comes into force on the day after the date on which it receives the Royal assent.*

[5] The Executive Summary of page 13 of the Explanatory Notes on the Bill concludes: "The current regulatory regime does not enable the Government or the public to identify all financial sector providers or their services, does not comply with the FATF Recommendations, and does not meet the objectives set out below. The information

[5] These Parts and sections of the Bill are: Part 2. Registration, and S44. Financial service provider must be a member of an approved dispute resolution scheme. Sub-part 2. Approval of dispute resolution schemes S45- 64. Sub-part 3. Reserve Scheme. S65-70.

available on the range of financial services an entity provides is not easily accessible to investors and is not comprehensive. The system has led to negative comments on New Zealand's level of compliance with international standards. Therefore it is not appropriate to maintain the status quo."[6] The comparatively low rates of national and household savings are well documented,[7] and the recent collapse of more than a dozen large and small finance companies is a harsh reminder of the intertwining of the sector with the daily lives of our citizens. Appropriate regulation of the financial sector would build a solid foundation for improving consumer awareness and confidence, and would reduce the risks of participation in the sector. More importantly, appropriate regulation of the financial sector will reduce and eventually eliminate the loan sharks who are currently exploiting our poorest and most vulnerable communities, and undermining the valuable contribution made by principled suppliers of financial products and services.

[6] Membership of an approved dispute resolution scheme will become mandatory for financial services providers only if, or when, a reserve scheme is created in addition to the existing or newly created resolution schemes. Some financial service providers will delay becoming members of these schemes, thus blocking access to dispute resolution funds for their customers. Such providers may well be those who operate at the fringes and whose customers are the most vulnerable.

Recommendations

- that the Act come into force, with the register in place, in 2008.

- that if there are providers who have not become members of a scheme within 1 year from the commencement of this Act, then they are assigned to a reserve scheme.

(2) The proposed imposition of a charge on consumers for dispute resolution

[7] Steps have been taken to minimise costs for financial product and service providers, as the Explanatory Notes to the Bill state on p. 31:

[6] pdf: DBHOH_BILL_8376_568991, downloaded 05 February 2008 from http://www.parliament.nz
[7] For example, in Skilling, D. and D. Boven (2005). Discussion Paper 2005/4 *Dancing With The Stars*. Auckland, The New Zealand Institute.

Steps taken to minimise compliance costs

The existence of multiple dispute resolution schemes will allow firms to seek out the scheme that has the best fit. This will minimise costs for firms in complying with the scheme's rules.

The criteria for approval of a scheme have been designed with a principles-based approach so as to give schemes flexibility to meet the requirements in the best way for them, that is, the cheapest and most effective.

[8] At the same time, the Bill proposes the introduction of costs to consumers for dispute resolution. S47 Mandatory considerations for approval [of a scheme] includes:

S47 (1) (g) The cost, if any, to lodge a complaint with the scheme, and whether that cost is reasonable and appropriate.

[9] Moreover, in S58:

58 Rules about approved dispute resolution scheme

The person responsible for an approved dispute resolution must issue rules about that scheme, and those rules must provide for, or set out the following:

S58 (i) *any provision for allocating the costs of resolving the dispute between the member complained about and the complainant…*

[10] This implies some sort of cost sharing such as occurs in some cases heard within the court systems. The impact of such a measure would establish a significant barrier to potential complainants. The imbalance between an individual consumer and a service provider with greater financial resources or insurance cover makes such a sharing of costs unreasonable and unfair. As we have noted above, the existing schemes are industry-funded as a service to consumers.

Right of appeal S58 (j) and sections 71 to 73

[11] In the existing Schemes a decision on a complaint, if accepted by the complainant, is binding on the scheme member but if the complainant is dissatisfied they may take court action. As this clause is worded, in any appeal to the court system by the scheme member, the complainant is the other party. The role of the dispute resolution scheme is limited to the provision of a report on the matter. Thus the weight of opposing the appeal would rest on the complainant, who would need to engage legal representation. In such a circumstance the complainant is most likely to give up on the matter. This undermines the reason for setting up the dispute resolution schemes in the first place.

[12] The current Banking and Insurance and Savings Ombudsman industry-funded Schemes have operated their dispute resolution services for over 11 years as a free service to consumers. This has ensured that a fair process is accessible to consumers who have a complaint that has not been resolved by the service provider. We do not support creating the potential for schemes to impose a cost on people wishing to make a complaint. Making a complaint requires considerable effort and time for a consumer. Those who are making a complaint are likely to have or perceive financial loss or hardship because of the actions of the provider. The imposition of a charge or fee would be placing a further burden on them. In order not to create a deterrent to making a complaint, any consumer charge or fee would need to be set so low it would be unlikely to cover the cost of administering a fee system.

Recommendations

- that S47 (1) (g) is changed to ensure that there is no cost to the consumer for dispute resolution under the schemes.

- that S58 (i) is changed to exclude sharing the costs of dispute resolution.

- that S71 to 73 be revised to provide for a judicial review of the scheme's process as recourse for a scheme member who perceives disadvantage from a faulty or unfair process.

(3) The need for consumer representation in schemes' governance

Recommendations

- Under *Consultation with members and consumers S47 (1)(b),* and *(d) Governance arrangements,* the Crown can establish conditions for registration, and guidelines on appropriate and effective consumer consultation to assist those groups seeking to establish a new scheme. Such guidelines would include the need to consult about rule changes in the future. We strongly recommend that the Bill states that independence and accountability in governance arrangements must be embodied by equal representation of industry and those consumers described in S44 (a) (i), (ii), with an independent chair.

Recommendations

- S58 *Rules about approved dispute resolution scheme* could include the separation/independence of the scheme's decision-making on individual complaints, from the governance structure of the scheme. There is a strong case also for the governance structure of the schemes to support the development and maintenance of members' internal complaint handling systems.

(4) The risks posed by multiple schemes

[13] The Bill makes no specific reference to the basis on which financial service providers might come together to form a scheme or to become members of an existing scheme. The Insurance and Savings and Banking Ombudsman's Schemes are based on industry groupings. Schemes on product lines or particular activities mean one provider could be a member of multiple schemes. This would create confusion for consumers.

[14] Also, a multiplicity of small schemes is not in the interests of consumers. The more schemes there are, the greater the likelihood for confusion. Smaller schemes with few complaints are unlikely to develop the expertise in dispute resolution or an in-depth industry-specific knowledge, thus weakening the effectiveness of the scheme. The Australian experience following financial service industry regulation has increasingly shown a broadening in scheme membership and scheme mergers.

[15] In addition, there should be limited capacity for a provider to move from one scheme to another. Otherwise, a member who has had many complaints against them upheld, might seek to move to an alternative scheme perceived to be more favourable to their perspective. Differences in the cost to members of different schemes may encourage scheme swapping and create either competition among schemes or cost-cutting to the detriment of the service offered to complainants.

[16] Allied to the consumer confusion inherent in multiple schemes is the problem with defining the dispute. S58 (e) implies that the complainant needs to focus on a complaint centring on the breaches set out in (i) – (iii). Complainants often have difficulty formulating their complaint clearly. This requirement undermines the concept of a fair dispute resolution process.

Recommendations

- that scheme membership be based on industry groupings.
- that scheme registration requires a of a minimum number of members.
- that there is a prohibition on scheme-hopping.
- that S58 (e) is changed to state that dispute resolution schemes may determine complaints only within the listed categories.

(5) The need for public awareness of the newly introduced consumer protections

Notification and publication of decision – s49 (b)

Recommendations

- We suggest that the section dealing with the notification and publication of any decisions of the Minister on the approval of new schemes be strengthened by the inclusion of a requirement to advise certain community and consumer groups who are likely to provide information to consumers on financial services matters. The Ministry of Consumer Affairs could be charged with maintaining a list of consumer and community groups (including the National Association of Citizens Advice Bureaux, the Federation of Family Budgeting Services, the Coalition of Community Law Centres, Consumer NZ). We suggest the insertion of a new subsection 49 (b) (iii), with wording that could read as below or similar:

> (iii) notified to certain consumer and community groups, on the advice of the Ministry of Consumer Affairs or any other government department that for the time being has responsibility for the administration of the Fair Trading Act.

We would also support a corresponding amendment to s 55 (c) (iii) dealing with notification and publication of withdrawal of approval.

Responsibility for informing people about the scheme S58 (o)

[17] Informal research suggests members are not adequately informing consumers of the existing dispute resolution services, despite requirements within their respective codes to do so. Both the industry-focused ombudsmen are involved in forums with community organizations and undertake other activities to build knowledge of the schemes within the wider community. Although a single 0800 number would make it easy for a complainant to be referred to the appropriate scheme, and such a system would provide economies of scale for promotional activity about the availability of the services, this is not in place at present, and there is no provision for it in the Bill. The wide range of financial service providers and the varying capacity and resourcing of the dispute resolution schemes that will be approved under the provisions of this Bill make the single 0800 number even more beneficial to consumers.

Recommendations

- that scheme members are required to inform their consumers about the scheme.

- that schemes develop a single 0800 number for all complaints.

- that the Crown ensure that a public education campaign informs consumers of the regulatory changes, their rights, and their access to dispute resolution and redress in the financial sector.

Summary

[18] Child Poverty Action Group's submission recommends:

- full implementation of the dispute resolution scheme and register in 2008
- no charge or fee to consumers for dispute resolution
- consumers and the industry are equally represented in schemes' governance
- the risks posed by multiple schemes are minimised
- a comprehensive public awareness campaign marks the passing of the Bill into law.